

Message Text

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FM AMEMBASSY OTTAWA

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C O N F I D E N T I A L OTTAWA 1389

LIMDIS

E.O. 11652: GDS

TAGS: EMIN, EINVA, CA

SUBJ: SASKATCHEWAN POTASH

1. SUMMARY. THREE DEVELOPMENTS MAKE IT DESIRABLE TO HAVE A NEW, SYSTEMATIC LOOK AT HOW ER SHOULD HANDLE THE POTASH DISPUTE. THIS MESSAGE ASKS FOR A REVIEW BY THE CIEP EXPROPRIATIONS COMMITTEE IN ORDER FOR THE US TO BE READY TO ACT PRIOR TO ANNOUNCEMENT OF THE FIRST TAKEOVER, WHICH MAY OCCUR AS EARLY AS THIS MONTH.

2. THE THREE DEVELOPMENTS ARE AS FOLLOWS:

3. FIRST, OTTAWA'S RESPONSE TO OUR NOTE (OTTAWA 1175) SEEMS TO SIGNAL A NOLO CONTRENDERE ATTITUDE BY THE FEDERAL GOVERNMENT. IN RECENT CONVERSATIONS WITH THE AMBASSADOR, MINISTERS HERE HAVE BEEN TAKING A LESS AND LESS VIGOROUS ATTITUDE ON THE SASKATCHEWAN TAKEOVER. FOR TAX, INVESTMENT POLICY, AND EVEN CONSTITUTIONAL REASONS THEY DON'T LIKE IT, BUT THEY APPEAR ANXIOUS TO AVOID A BRAWL WITH SASKATCHEWAN AT THIS POINT.

4. SECOND, PREMIER BLAKENEY'S EFFORT TO NEGOTIATE WITH THE COMPANIES SEEMS TO BE GAINING MOMENTUM. PRESIDENT LENON OF IMC TOLD THE AMBASSADOR ON MARCH 30 THAT HE EXPECTS BLAKENEY TO SUCCESSFULLY COMPLETE POTASH TAKEOVER NEGOTIATIONS WITH THREE COMPANIES, DUVAL CORP. OF CANADA, SYLVITE
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(HUDSON MAY MINING AND SMELTING'S POTASH DIVISION), AND THE

FRENCH-GERMAN COMPANY OF ALWINSAL. ACCORDING TO LENON, BLAKENEY MIGHT BE READY TO ANNOUNCE A TAKEOVER OF DUVAL BY THE END OF APRIL OR IN MAY. SUCH ACTION WOULD BE IN ACCORD WITH BLAKENEY'S PROPOSED TIMETABLE AS ANNOUNCED IN HIS MARCH 4 SPEECH IN OTTAWA TO THE CANADIAN FERTILIZER INSTITUTE (SEE OTTAWA 916). OTHER SOURCES (SEE TORONTO A-29 OF APRIL 1) REPORT OTHER POSSIBLE DEALS AND ERODING UNANIMITY ON THE PART OF MEMBERS OF THE POTASH PRODUCERS ASSOCIATION.

5. THIRD, BLAKENEY REMAINS UNCERTAIN AS TO WHAT WE MAY DO, AND IS SIGNALING WILLINGNESS TO TALK WITH THE US GOVERNMENT (SEE OTTAWA 1311).

6. AS WE SEE IT, U.S. OBJECTIVES IN FACE OF SASKATCHEWAN'S ACTION SHOULD BE:

(A) TO DEVISE PROTECTIVE MEASURES AGAINST THE POSSIBILITY OF MONOPOLY BEHAVIOR IN THE POTASH INDUSTRY;

(B) TO ISOLATE, AS MUCH AS POSSIBLE, THE POTASH ACTION TO AVOID THE POSSIBILITY OF SPILLOVER EFFECTS LEADING TO A RASH OF TAKEOVERS OF THIS TYPE IN OTHER SECTORS AND PROVINCES; AND,

(C) TO INSURE FULL, PROMPT AND EFFECTIVE PAYMENT TO U.S. COMPANIES FOR ANY PROPERTIES BOUGHT IN OR EXPROPRIATED.

7. TO ACHIEVE THESE OBJECTIVES, THE FOLLOWING POTENTIAL INSTRUMENTS ARE AVAILABLE:

(A) THREAT OR FACT OF DIVERSIFICATION OF US SUPPLIES. SOME DIVERSIFICATION FROM OUR 65 TO 70 PERCENT DEPENDENCY ON SASKATCHEWAN POTASH WOULD APPEAR DESIRABLE REGARDLESS OF WHAT BLAKENEY MAY DO. WE UNDERSTAND THAT POTASH IMPORT DISCUSSIONS WITH USSR EXPORTERS ARE CURRENTLY IN ABEYANCE, GIVEN THE PRESENT GLUT OF POTASH SUPPLIES AND PENDING IMPORTER DISCUSSIONS WITH BLAKENEY. THE CRITICAL THING, HOWEVER, IS NOT WHAT US IMPORTERS DO NOW BUT WHAT THEY DO 18 TO 24 MONTHS FROM NOW WHEN THE GLUT WILL

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BE WORKED OFF.

(B) US ANTI-TRUST ACTION. WE SHOULD CONSIDER WHAT POWERS ARE REALISTICALLY AVAILABLE TO RESPOND TO MONOPOLY-TYPE ACTION AMONG PRODUCERS IN FIXING THE PRICE ON EXPORTS TO THE US. BLAKENEY HAS NOTED, FOR EXAMPLE, THAT PRESSURES FROM THE USG HAVE SERIOUSLY HAMPERED EFFORTS BY THE INDUSTRY'S OFF-SHORE MARKETING

ORGANIZATION CANPOTEX TO SELL CANADIAN POTASH IN SUCH MARKETS AS JAPAN. BLAKENEY SAID "WE THINK THIS IS AN ODD SITUATION FOR AN INDEPENDENT COUNTRY LIKE CANADA TO FIND ITSELF IN" AND HAS USED THIS SITUATION AS AN ADDITIONAL ARGUMENT FOR TAKING OVER THE INDUSTRY.

(C) SASKATCHEWAN'S BORROWING ACCESS TO THE NEW YORK FINANCIAL MARKET. WE NEED A CAREFUL ANALYSIS OF THE FINANCIAL SITUATION OF THE PROVINCE AND ITS CASH FLOW; THE IMPACT OF THE ON-GOING DISPUTE BETWEEN THE INDUSTRY AND THE GOVERNMENT OVER THE RESERVES TAX ON THE CASH FLOW; THE KIND OF BORROWING SASKATCHEWAN WOULD HAVE TO DO IN ORDER TO BUY OUT THE FIRMS WITH WHICH IT IS CURRENTLY NEGOTIATING; AND THE PLACES IN WHICH THE MONEY COULD BE FOUND. (NEW YORK BANKS WHICH HAVE DONE OR ARE DOING BUSINESS WITH SASKATCHEWAN WOULD PROBABLY BE THE BEST SOURCES OF SUCH INFORMATION.) WAYS AND MEANS BY WHICH WASHINGTON AGENCIES INFLUENCE ACCESS TO THE NEW YORK FINANCIAL MARKET SHOULD ALSO BE EXAMINED. THE THIS REGARD SALOMON BROTHERS PARTNER SCHMEELK TOLD AMBASSADOR APRIL 1 THAT HE STILL DOUBTED THAT SASKATCHEWAN COULD PICK UP MORE THAN \$200 MILLION FOR "EXPROPRIATION FINANCING" IN NEW YORK. A MAJOR LINE OF CREDIT, ACCORDING TO SCHMEELK, WOULD REQUIRED PARTICIPATION BY THE BIG NEW COMPANIES, WHICH HE JUDGED UNLIKELY TO PARTICIPATE IF THERE WERE AN INVESTMENT DISPUTE INVOLVED. (BROWN BROTHERS REP CURRENTLY VISITING CANADA THIS WEEK COMMENTED TO EMBOFF THAT SASKATCHEWAN HAS STRONG CREDIT RATING AND, WHILE NEW YORK FINANCIAL COMMUNITY DOES NOT FEEL COMFORTABLE ABOUT POTASH ACTION, IT IS IMPRESSED BY BLAKENEY AND WAY IN WHICH HE HAS MANAGED PROVINCE'S FINANCES).

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(D) DETERRENT ACTION BY THE GOC. THE MAIN INSTRUMENT HERE WOULD SEEM AT FIRST VIEW TO BE TO DENY THE CROWN CORPORATION, POTASH CORP. OF SASKATCHEWAN, FEDERAL TAX EXEMPTION. WHILE THERE IS A GOOD DEAL OF SENTIMENT IN OTTAWA TO DO JUST THAT, THE POLITICAL REALITIES ARE THAT OTTAWA HAS ENGAGED THE PROVINCES IN A RUNNING BATTLE FOR TWO YEARS NOW OVER RESOURCE TAXATION AND MIGHT HAVE LITTLE STOMACH TO PROVOKE A FURTHER CONSTITUTIONAL ROW OVER TAXATION OF CROWN ENTITIES. POSSIBILITY THAT TRUDEAU MAY "PATRIATE" THIS CONSTITUTION IN THE FACE OF PROVINCIAL OPPOSITION MAKES THIS ALL THE MORE TRUE.

8. AS SEEN FROM HERE, NEXT IMPORTANT PLAY MAY BE IN LATE APRIL ANNOUNCEMENT BY BLAKENEY OF DEAL WITH AT LEAST ONE OF THE COM-

PANIES, PRIOR TO HIS MAY 3 DEPARTURE FOR THE PEOPLE'S REPUBLIC OF CHINA. WE SHOULD HAVE OUR TACTICS AGREED WELL BEFORE THAT. IN OUR VIEW, THOSE TACTICS SHOULD INCLUDE:

(A) APPROACH THE FEDERAL GOVERNMENT HERE ASKING WHAT ITS ATTITUDE WILL BE IN THE EVENT OF TAKE-OVER ON THE TAX STATUS OF THE RESULTING CROWN CORPORATION, SINCE THE ATTITUDE COULD HAVE AN IMPORTANT BEARING ON THE SCOPE, FINANCING AND SPEED OF TAKEOVER;

(B) ENCOURAGE US IMPORTERS TO RESUME DISCUSSION OF SOURCE DIVERSIFICATION WITH THE USSR FOCUSING ON THE PERIOD 18-24 MONTHS FROM NOW WHEN THE PRESENT GLUT MAY BEGIN TO WEAR OFF;

(C) CONSIDER COMMUNICATING TO THE FEDERAL GOVERNMENT AND TO SASKATCHEWAN POTENTIAL CONSEQUENCES FOR POTENTIAL ANTI-TRUST IMPLICATIONS OF TAKEOVER OF ONE-HALF OF THE INDUSTRY;

(D) CONSIDER REQUESTING WALL STREET COMPAINES THAT NORMALLY FINANCE SASKATCHEWAN TO BE IN TOUCH WITH THE TREASURY DEPARTMENT PRIOR TO GOING AHEAD WITH ANY SIGNIFICANT NEW SASKATCHEWAN FINANCING.

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9. EMBASSY WILL PROVIDE ANALYSIS OF SASKATCHEWAN FINANCES PER PARA 7(C) ABOVE. REQUEST THAT CIEP EXPROPRIATIONS COMMITTEE REVIEW THE DISPUTE AND OUR STRATEGY IN RESPONDING TO IT. ENDERS

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